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Nos. 08-240 and 08-372

In the Supreme Court of the United States

MAC'S SHELL SERVICE, INC., ET AL., PETITIONERS

v.

SHELL OIL PRODUCTS COMPANY LLC, ET AL.

SHELL OIL PRODUCTS COMPANY LLC, ET AL., PETITIONERS

v.

MAC'S SHELL SERVICE, INC., ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONERS IN NO. 08-372 AND RESPONDENTS IN NO. 08-240

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QUESTIONS PRESENTED

The Petroleum Marketing Practices Act (PMPA or Act), 15 U.S.C. 2801 *et seq.*, limits the circumstances in which petroleum refiners or distributors may "terminate" a franchise or "fail to renew" a franchise relationship involving the sale or supply of motor fuel.

In No. 08-372, *Shell Oil Products Co. LLC* v. *Mac's Shell Service, Inc.*, the question presented is whether a franchisee may recover for "constructive termination" under the PMPA when it continues to operate the franchise by purchasing the same fuel, reselling it under the franchisor's trademark, and occupying the leased marketing premises.

In No. 08-240, *Mac's Shell Service, Inc.* v. *Shell Oil Products Co. LLC*, the question presented is whether a franchisee who signs a renewal agreement "under protest" and operates under the terms of the agreement may maintain a claim for "constructive nonrenewal" under the Act.

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BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONERS IN NO. 08-372 AND RESPONDENTS IN NO. 08-240

INTEREST OF THE UNITED STATES

The questions presented in these cases concern the scope of the restrictions on termination and nonrenewal in the Petroleum Marketing Practices Act (PMPA or the Act), 15 U.S.C. 2801 *et seq.* The Department of Energy is responsible for summarizing the relevant provisions of the PMPA in the Federal Register. See 43 Fed. Reg. 38,743 (1978); 61 Fed. Reg. 32,786 (1996). Because the scope of the Act may affect competition in petroleum marketing, this case is of concern to the Antitrust Division of the United States Department of Justice. At the Court's invitation, the United States filed a brief as amicus curiae at the petition stage of these cases.

STATEMENT

1. The Petroleum Marketing Practices Act (PMPA or the Act), 15 U.S.C. 2801 *et seq.*, prohibits petroleum refiners and distributors from "terminat[ing]" any franchise involving the sale or supply of motor fuel "prior to the conclusion of the term, or [its] expiration," or from "fail[ing] to renew any franchise relationship," except for enumerated reasons and after written notice. 15 U.S.C. 2801(1)(A), 2802, 2804.[1] The Act defines the term "franchise" to include any contract allowing a retailer or distributor to use the franchisor's trademark, to purchase motor fuel for resale, or to occupy leased marketing premises. 15 U.S.C. 2801(1)(B). These three types of agreements are commonly described as the "statutory elements of the franchise." Pet. App. 3 n.1.[2] The term "franchise relationship" is defined as the parties' "respective motor fuel marketing or distribution obligations and responsibilities" in connection with the franchise. 15 U.S.C. 2801(2). "'[T]ermination' includes cancellation," and "fail to renew" means "a failure to reinstate, continue, or extend the franchise relationship." 15 U.S.C. 2801(14) and (17).

If a franchisor violates specified provisions of the PMPA, its franchisee may bring suit in federal district court. 15 U.S.C. 2805. The Act provides for a wide range of remedies, including compensatory damages, reasonable attorneys' fees and expert costs, punitive damages, and "such equitable relief" as the court deems necessary to address the statutory violation. 15 U.S.C. 2805(a), (b)(1), (d) and (e). The Act also requires district courts to grant preliminary injunctive relief preserving the status quo if the franchisee shows that the franchisor has terminated the

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[1] Special rules apply to trial and interim franchises. 15 U.S.C. 2803.

[2] Unless otherwise noted, all references to "Pet." and "Pet. App." are to the petition and appendix in No. 08 240.

franchise or failed to renew the franchise relationship, that "there exist sufficiently serious questions going to the merits to make such questions a fair ground for litigation," and that the balance of equities favors such relief. 15 U.S.C. 2805(b)(2). The PMPA preempts state law governing termination and nonrenewal to the extent such law is inconsistent with the Act. 15 U.S.C. 2806(a)(1).

2. Between 1982 and 1998, Shell Oil Products Co. LLC (Shell) offered its franchisees a rent subsidy called the Variable Rent Program (VRP). Pet. App. 3. That subsidy reduced the monthly rent by a set amount for every gallon of gasoline the franchisee sold above a specified threshold. *Ibid.* Shell renewed the subsidy in annual notices to franchisees. *Ibid.* Although the notices "explicitly provided for cancellation with thirty days' notice," various oral representations suggested that "the [s]ubsidy or something like it would always exist." *Id.* at 3-4.

In 1998, Shell and Texaco created a joint venture, Motiva Enterprises LLC (Motiva), to conduct their domestic gasoline marketing operations. Pet. App. 3. Shell assigned its rights and duties under the relevant franchise contracts to Motiva, which initially replaced the VRP with a different rent subsidy. *Ibid.* On January 1, 2000, however, Motiva ended that replacement subsidy, causing the Shell stations to pay more rent. *Id.* at 4.[3] Motiva did not include the subsidy in the new leases it offered Shell franchisees when their franchise agreements expired. *Ibid.*[4]

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[3] The amount of the rent increase following the elimination of the subsidy varied by dealer. Compare, *e.g.*, J.A. 339 (annual rent for Mac's Shell Southbridge station increased from $61,784 to $64,893), with J.A. 336 (annual rent for Karol's station increased from $59,447 to $99,120).

[4] In addition to eliminating the subsidy, the new Motiva leases changed the way in which rent was computed (using an asset-based methodology similar to the one that Texaco had used before the creation of Motiva). J.A. 218, 236-238. For some stations, annual rent was

3. On July 27, 2001, 63 Shell dealers filed suit in federal district court, asserting state and federal claims. The dealers principally alleged that their property leases had incorporated the rent subsidy and that the elimination of the subsidy breached those leases. Pet. App. 5-6. In addition to alleging violations of their state-law contract rights, the dealers asserted that Shell's and Motiva's conduct had violated two provisions of the PMPA. First, the dealers alleged that Shell had "constructive[ly] terminat[ed]" their franchises, in violation of 15 U.S.C. 2802(a)(1), by assigning the contracts to Motiva and eliminating the rent subsidy. Pet. App. 6. Second, the dealers claimed that Motiva's offer of new contracts without the rent subsidy amounted to a "constructive nonrenewal" of their franchise relationships, in violation of 15 U.S.C. 2802(a)(2). Pet. App. 6, 27. The dealers contended that a constructive nonrenewal had occurred even though they had in fact signed renewal agreements, because they had done so "under protest." *Id.* at 27.

On July 30, 2003, the dealers moved for a preliminary injunction under the PMPA. The district court denied the motion, explaining that because the dealers had "waited years before seeking preliminary injunctive relief," the court was unable to "turn the clock back" and "preserve the status quo." Pet. App. 49-50 (citation omitted).

After a 15-day trial involving eight dealers selected by the court, the jury found against Shell and Motiva on all claims and awarded the dealers $3.3 million, including $1.3 million on the constructive termination claim and $1.2 million on the constructive nonrenewal claim. J.A. 376-386.

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less under the new Motiva leases than under the preexisting leases after elimination of the subsidy. See, *e.g.*, J.A. 316-318, 339 (Mac's Shell Southbridge signed a new Motiva lease in October 2001; its annual rent decreased to $56,600 in 2002); J.A. 314-315, 336 (Karol signed a new Motiva lease in December 2000; her station's annual rent decreased to $66,371 in 2001).

Both before and after the verdict, the defendants moved for judgment as a matter of law on the dealers' constructive termination and constructive nonrenewal claims, noting that seven of the eight dealers had signed and operated under renewal agreements and that four of the eight dealers were still operating their stations at the time of trial. J.A. 212-213, 391-396. The district court denied the motions, 08-372 Pet. App. 34a-54a, 58a-59a, and the defendants appealed, Pet. App. 2.

4. The court of appeals affirmed in part and reversed in part. Pet. App. 1-41. On the PMPA claims, the court affirmed the judgment on the constructive termination claim but reversed the judgment on the constructive nonrenewal claim. *Id.* at 20-32.

a. In sustaining the jury verdict on the constructive termination claim, the court of appeals explained that a franchisee may establish a violation of Section 2802(a)(1) by showing that, as a result of assigning the franchise, "the franchisor breached one of the three statutory components of the franchise agreement (the contract to use the refiner's trademark, the contract for the supply of motor fuel, or the lease of the premises)." Pet. App. 20-21 (citation omitted). The court concluded that the dealers had made that showing because they had "prove[d] to the jury's satisfaction" that, by eliminating the rent subsidy, "Motiva breached the lease component of the franchise agreements." *Id.* at 21.

The court of appeals rejected the defendants' argument that, to constitute a constructive termination under the PMPA, any "breach must amount to a total deprivation of one of the three elements of the franchise." Pet. App. 22; see *id.* at 24. The court held that the "appropriate threshold" for a constructive termination claim was reflected in the jury instructions given in this case, which stated that the breach must constitute "such a material change that it effectively ended the lease, even though the plaintiffs continued

to operate the business." *Id.* at 23. The court acknowledged that the doctrines of constructive discharge in employment law and constructive eviction in landlord-tenant law "require an actual severance of the relationship: [t]he employee must leave the workplace; the tenant must move out." *Id.* at 22-23. The court concluded, however, that such a rule should not apply under the PMPA because "sunk costs, optimism, and the habit of years might lead franchisees to try to make the new arrangements work, even when the terms have changed so materially as to make success impossible," and the "congressional plan would be frustrated by requiring a franchisee to go out of business before invoking the protections of the PMPA." *Id.* at 23 (citation omitted).

b. The court of appeals reversed the judgment of liability on the constructive nonrenewal claim, concluding that the PMPA does not encompass such a claim "where the franchisee has signed and operates under the renewal agreement complained of." Pet. App. 27-32. Citing the structure of the PMPA, which requires notice of nonrenewal and permits the franchisee to seek preliminary injunctive relief under a relaxed standard, the court explained that "Congress intended to limit the reach of the PMPA to cases where either a notice is given or an actual nonrenewal has taken place." *Id.* at 28. The court therefore concluded that the Act "requires that franchisees faced with objectionable contract terms refrain from ratifying those terms by executing the contracts (even 'under protest')." *Id.* at 30.

Because in this case "the Dealers signed the new agreements 'under protest' and continued in operation under the new agreements," Pet. App. 30, the court of appeals held that they could not claim constructive nonrenewal. Were the rule otherwise, the court explained, a "franchisee [could] sign the contract and simultaneously challenge it," giving the franchisee the benefit of the contract with nothing to lose "[i]f its claims were rejected by the courts." *Ibid.* In

the court's view, that result would violate "the balance Congress has struck" in the PMPA. *Id.* at 30-31.

SUMMARY OF ARGUMENT

I. The court of appeals erred in upholding the jury verdict in the dealers' favor on their "constructive termination" claim.

A. Under any usual understanding of the PMPA's language, a franchisor does not "terminate" a franchise (15 U.S.C. 2802(a)(1)) unless it brings at least one statutory element of the franchise to an end. A franchisor may terminate the franchise explicitly by formally ending the agreement, or it may do so "constructively" by engaging in conduct that effectively forces the franchisee to abandon the franchise. In either case, however, the franchisor's conduct must actually cause the franchise to come to an end. The text of the Act leaves no room for the court of appeals' expansive conception of "constructive termination," under which a franchise is "treated" as "terminated" even though the challenged conduct does not prevent the franchisee from continuing to exercise all three prerogatives the franchise entails.

B. The court of appeals viewed its interpretation as necessary to effectuate the Act's overarching purposes. Because the statutory text is unambiguous, that type of analysis was unwarranted. In any event, the purpose, structure, and history of the PMPA do not support the court of appeals' holding.

The Act is a compromise measure that reflects a delicate accommodation of the competing interests of franchisors and franchisees. Expanding the Act's coverage to conduct that does not "terminate" the franchise would upset that balance. The court of appeals' concern that a literal reading would leave franchisees without adequate recourse to challenge unlawful conduct ignores the availability of both pre-

liminary injunctive relief under the Act and state-law remedies that Congress deliberately left in place. And the court of appeals' indeterminate, internally contradictory, and unworkable standard, under which a franchise that is ongoing in each of its basic components nevertheless can be declared "effectively ended," runs contrary to Congress's goal of providing franchisees with predictable and nationally uniform results.

C. The court of appeals' approach is also inconsistent with the understanding of "constructive termination" that courts have developed in other contexts. As the court of appeals recognized, the common-law analogues of that doctrine have traditionally "require[d] an actual severance of the relationship." Pet. App. 23. Courts have generally applied the concept of "constructive termination" to encompass conduct that forces an actual end to the relationship, even though it does not take the form of an express or formal termination. The court of appeals offered no sound basis for applying a more expansive understanding of that concept to the PMPA.

D. The dealers failed to establish that their franchises were "terminated" within the meaning of the Act. All eight dealers continued to avail themselves of the statutory elements of the franchises long after the rent subsidy was eliminated. That continued operation precluded any reasonable finding that the withdrawal of the subsidy effectively compelled the dealers to abandon their businesses.

II. The court of appeals correctly held that a franchisee cannot assert a claim for "nonrenewal" under the Act after it has signed and operated under a renewal agreement. As a matter of plain language, there is no "failure to renew" when the franchisor has in fact continued the franchise relationship by offering a new agreement that the franchisee has accepted. The dealers contend that they preserved their rights under the PMPA by signing the renewed agreements

"under protest." But a dealer who enters into a new franchise agreement despite dissatisfaction with its terms has nonetheless "renewed" the franchise relationship and therefore has no cause of action for "nonrenewal" to preserve.

The structure and purpose of the Act confirm that understanding of the term "fail to renew." As part of Congress's accommodation of the interests of franchisors and franchisees, the Act permits franchisors to make efficient marketing and distribution changes at the time of renewal, while affording franchisees that object to such modified terms a procedural mechanism to obtain preliminary injunctive relief preserving the status quo while the dispute is in litigation. That balance would be seriously undermined if franchisees could sign a renewal agreement "under protest," continue operating the franchise under the new terms, and then later challenge the renewal agreement as a "constructive nonrenewal."

Contrary to the dealers' contention, a franchisee presented with a coercive offer to renew has options beyond agreeing to the franchisor's proposed terms or going out of business. A franchisee in those circumstances may reject the offer and obtain injunctive relief preventing a threatened nonrenewal from taking effect. There is no merit to the dealers' argument that the PMPA's injunctive remedy is inadequate because franchisees lack the resources promptly to seek such relief. The Act allows successful dealers to recover attorneys' fees, expert costs, compensatory damages, and, in some circumstances, punitive damages. 15 U.S.C. 2805(d)(1). Such provisions are normally considered sufficient to encourage suit.

The evidence at trial showed that seven dealers signed renewal agreements, and that the eighth sold his franchise before the existing agreement expired. The dealers therefore did not establish that the defendants "fail[ed] to renew" their franchise relationships, and the court of appeals cor-

rectly granted judgment in the defendants' favor on the constructive nonrenewal claims.

ARGUMENT

I. A FRANCHISEE MAY NOT RECOVER FOR "CONSTRUCTIVE" TERMINATION IF IT CONTINUES TO SELL THE SAME FUEL, USE THE SAME TRADEMARK, AND OCCUPY THE SAME PREMISES

The court of appeals held that "a breach of the franchise agreement need not result in complete deprivation of a statutory element of the franchise to support a constructive termination" claim under 15 U.S.C. 2802(a)(1). Pet. App. 24. That conclusion was incorrect. Under any usual understanding of the statutory language, a franchisor can be said to "terminate" an existing franchise, "constructively" or otherwise, only when it forces an end to the franchisee's purchase of the franchisor's fuel, its use of the franchisor's trademark, or its occupation of the leased marketing premises. Because the dealers in this case continued to exercise each of those three prerogatives long after the defendants withdrew the rent subsidy, the defendants did not "terminate" the franchises in violation of the PMPA.

A. The Prohibition Imposed By 15 U.S.C. 2802(a)(1) Is Limited By Its Terms To Franchisor Conduct That Terminates The Franchise

The PMPA does not federalize all contract disputes between petroleum companies and their franchisees or establish general federal standards of fair dealing in petroleum marketing. Rather, it addresses only a narrow category of conduct. *Inter alia*, the Act provides that, except for specified reasons, a motor-fuel franchisor may not "terminate any franchise" before its expiration date. 15 U.S.C. 2802(a)(1). The Act defines the term "franchise" to encompass "a set of definite agreements" concerning the lease of the marketing

premises, the supply of the franchisor's motor fuel, and the use of the franchisor's trademark. Pet. App. 7-8; 15 U.S.C. 2801(1)(B).

1. The scope of the prohibition on unlawful terminations is evident from the plain language of the PMPA. "Terminate" is a well-understood term that had the same meaning when Congress enacted the PMPA in 1978 as it has now: "bring to an end." *The Random House Dictionary of the English Language* 1465 (1st ed. 1966). Consistent with that common understanding, Congress provided in the PMPA that "[t]he term 'termination' includes cancellation," 15 U.S.C. 2801(17), a word that similarly denotes an end or nullification. Thus, a franchisor "terminate[s]" a "franchise" under the PMPA only by engaging in conduct that brings to an end at least one of the three statutory components of the franchise.

A franchisor typically terminates a franchise by explicitly ending one or more of the franchise elements prior to the expiration date. Even without such an explicit abrogation, however, the franchisor could "terminate" the franchise within the meaning of Section 2[illegible]a)(1) by engaging in conduct that effectively forces an end to one of the statutory elements. Thus, a franchisor could terminate a franchise by offering the franchisee fuel only on terms so disadvantageous as to amount to a refusal to supply, or by taking actions that, as a practical matter, prevent the franchisee from continuing to occupy the leased premises. In those circumstances, the "termination" might be termed "constructive," although the term "informal" is more accurate. See *Dersch Energies, Inc.* v. *Shell Oil Co.*, 314 F.3d 846, 864 n.17 (7th Cir. 2002) ("In the context of the PMPA, constructive means 'not directly expressed, but inferred,' *The Compact Oxford English Dictionary* 322 (2d ed. 1989), i.e., an indirect or informal termination or nonrenewal."). Under any circumstances, however, the franchisor's conduct does not fall within the statutory

prohibition unless it has the effect of ending at least one of the three prerogatives that the franchise entails.

2. The court of appeals adopted an expansive conception of "constructive termination" that cannot be reconciled with the plain meaning of the Act. The court of appeals held that a "constructive termination" occurs when a contractual breach is so "material" that it should be "treat[ed]" as a "termination of the franchise," Pet. App. 23, 26, even though there is neither an "actual abandonment" of the franchise nor an end of any of its elements, *id.* at 23. Thus, although the court purported to apply a standard requiring conduct that "effectively ended" the franchise, it upheld a verdict in the dealers' favor "even though the [dealers] continued to operate the business[es]" long after the rent subsidy had been withdrawn. *Ibid.* By holding that the elimination of the rent subsidy could violate Section 2802(a)(1) even though the dealers continued to occupy the leased premises, use Shell's trademark, and purchase Shell gasoline for resale, the court of appeals effectively expanded the scope of the statutory prohibition to encompass conduct that is unfavorable to the franchisee but does not "terminate" the franchise in any meaningful sense.

B. Extending The Statutory Prohibition To Conduct That Does Not Terminate The Franchise Is Inconsistent With The History, Structure, And Purposes Of The PMPA

The court of appeals viewed its interpretation of Section 2802(a)(1) as necessary to further Congress's goals in enacting the PMPA. Pet. App. 22-24. Even if the court's understanding of Congress's overall objectives in enacting the statute were correct, it would provide no sound basis for giving Section 2802(a)(1) a reading broader than its text will bear. See, *e.g.*, *Connecticut Nat'l Bank* v. *Germain*, 503 U.S. 249, 253-254 (1992). In any event, the court of appeals' analysis of Congress's aims was erroneous. Properly understood, the

purpose, history, and structure of the PMPA support the construction compelled by Section 2802(a)(1)'s text.

1. The court of appeals proceeded on an incomplete understanding of the PMPA's purpose and history. In the court's view, the Act was intended "to ensure that franchisees benefit from successful investment in their franchises." Pet. App. 24. The legislative history makes clear, however, that the PMPA was a compromise measure designed to "strike a balance between the at times conflicting interests of [franchisors and franchisees]." S. Rep. No. 731, 95th Cong. 2d Sess. 15 (1978) (*Senate Report*); see 123 Cong. Rec. 10,384 (1977) (statement of Rep. Brown) (the Act "represent[s] a delicate and effective compromise"); *id.* at 10,387 (statement of Rep. Dingell) ("[T]his bill is in a delicate state of balance."). Although Congress sought to redress "the disparity of bargaining power which exists between the franchisor and the franchisee," *Senate Report* 17, it also "recognize[d] the importance of providing adequate flexibility so that franchisors may initiate changes in their marketing activities to respond to changing market conditions and consumer preferences," *id.* at 19.

Section 2802(a)(1) reflects that balance. Congress sought to provide some protection for franchisees by limiting the circumstances in which franchisors can use or threaten the "extreme remedy" of ending the franchise. See *Senate Report* 18; *id.* at 15 ("The purpose of [the Act] is the establishment of minimum Federal standards governing the termination and nonrenewal of franchise relationships for the sale of motor fuel."); *id.* at 29 (suggesting that a franchisee could bring a claim under the PMPA where "the real estate lease or motor fuel supply agreement" was "terminat[ed]" or the trademark license was rendered "valueless"). At the same time, Congress declined "to create a federal common law for governing petroleum franchise agreements" or "to provide franchisees with a federal forum" to challenge conduct that,

although unfavorable to the franchisee, does not bring the franchise to an end. *Dersch Energies*, 314 F.3d at 861-862; see *id.* at 856 ("[T]he PMPA strikes a balance between the rights of franchisors and the rights of franchisees, by affording franchisees important but limited procedural rights, while at the same time providing franchisors with significant latitude to respond to changing market conditions."); *Esso Standard Oil Co.* v. *Department of Consumer Affairs*, 793 F.2d 431, 435 (1st Cir. 1986) ("Congress did not choose to use the PMPA to regulate the reasonableness of rents").[5]

The court of appeals emphasized the goal of franchisee protection to the exclusion of the countervailing goal of franchisor flexibility. As a result, the court stretched the prohibition on "termination" of franchises beyond the limited category of conduct, involving an actual end of the franchise, that Congress intended the Act to address. The decision below therefore upsets the delicate balance Congress struck. See *Burlington N. & Santa Fe Ry.* v. *United States*, 129 S. Ct. 1870, 1879 (2009) ("[L]iability may not extend beyond the limits of the statute itself.").

2. The court of appeals also misapprehended the remedies available to an aggrieved franchisee under the statutory scheme. The court concluded that franchisees must be per-

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[5] The dealers cite a portion of then-Judge Breyer's decision in *Veracka* v. *Shell Oil Co.*, 655 F.2d 445, 448 (1st Cir. 1981), stating that "[t]he legislative history of the [PMPA] shows that it[ ] * * * [sought] to prevent coercive or unfair franchisor practices." Pet. 11. But the legislative history the court cited in *Veracka* for that point, see *Senate Report* 17, 18, discussed Congress's efforts to limit "unfair terminations [and] nonrenewals." Nothing in that history reasonably suggests that Congress sought to prohibit other sorts of "unfair franchisor practices" or to treat those practices as terminations and nonrenewals, contrary to the most natural reading of the statute. In *Veracka* itself, the franchisor expressly indicated that it was not renewing the franchise, so these questions did not arise. See 655 F.2d at 447.

mitted to assert "constructive termination" even when the challenged conduct does not force an actual end to the franchise because "the congressional plan would be frustrated by requiring a franchisee to go out of business before invoking the protections of the PMPA." Pet. App. 23 (internal quotation marks and citation omitted). But that analysis ignores the existence of state-law remedies. The PMPA preempts any inconsistent state or local "law or regulation" governing the "termination" of a petroleum marketing franchise or the "nonrenewal" of a franchise relationship. 15 U.S.C. 2806(a)(1). Outside of those specific areas, however, Congress neither provided a federal remedy for breaches of franchise agreements nor limited States' authority to do so. See H.R. Rep. No. 737, 103d Cong., 2d Sess. 2-3 (1994) ("PMPA preemption does not extend to state regulation of underlying contract provisions."); *Senate Report* 42 ("State laws dealing with [other] aspects of the relationship are not preempted."). Thus, although Congress limited Section 2802(a)(1) of the PMPA to conduct that "terminate[s]" an existing franchise, state-law mechanisms remain available for breaches of contract that have less extreme consequences. The dealers' continued operations under the three essential elements of the franchise did not (as the jury's verdict on their state-law claims makes clear) prevent them from obtaining meaningful redress for the contract breaches that were found to have occurred. That continuing relationship simply remitted the dealers to state law to obtain relief on their contractual claims.

In any event, the court of appeals was simply incorrect in concluding that, if the word "terminate" in Section 2802(a)(1) is given its usual meaning, a franchisee must "abandon[] years of work and investment" before bringing a federal claim. Pet. App. 23. A franchisee who receives a notice of termination, or of imminent conduct that would effectively

force an end to a franchise element, can seek a preliminary injunction under 15 U.S.C. 2805(b)(2), enabling it to continue operating the franchise under the preexisting terms while the dispute is in litigation. Congress directed district courts to grant such relief if the franchisee demonstrates that "there exist sufficiently serious questions going to the merits to make such questions a fair ground for litigation," and that the balance of equities favors such relief. *Ibid.*[6] In an appropriate case, a franchisee therefore can make out a claim of constructive or informal termination without abandoning any of the basic components of its operation. This is not such a case, however, because the dealers "waited years before seeking" injunctive relief, "and at that point the court was obviously unable to "turn the clock back" and "preserve the status quo." Pet. App. 49-50 (quoting *Dersch Energies*, 314 F.3d at 863).

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[6] Section 2805(b)(2) also states that, to obtain injunctive relief, the franchisee must show that "the franchise of which he is a party *has been* terminated." 15 U.S.C. 2805(b)(2)(A)(i) (emphasis added). In common parlance, a franchisee who receives notice of an impending termination, or of conduct that would cause such a termination, "has been terminated" within the meaning of Section 2805(b)(2)(A)(i), just as an employee who has received a notice of termination that will be effective as of a date certain "has been terminated" from his employment. The requirement in Section 2805(b)(2) that the franchisee must show that its franchise "has been terminated" is therefore consistent with Congress's evident intent to permit franchisees to secure an injunction preventing a threatened termination from taking effect. See 123 Cong. Rec. at 10,383 (statement of Rep. Dingell); *id.* at 10,384 (statement of Rep. Long). It would make little sense for Congress to provide expressly for preliminary injunctive relief but require that the injury actually occur before such relief can be granted. Cf. *Lippo* v. *Mobil Oil Corp.*, 776 F.2d 706, 720 (7th Cir. 1985) (noting that "[i]n an action brought under section 2805(a) the franchisee has the burden of proving termination of the franchise" and that "[t]his must really mean attempted termination if the injunctive relief is to be of any use").

3. The decision below contravenes Congress's intent in an additional respect. The PMPA reflects Congress's effort to establish "a single, uniform set of rules" governing the termination of petroleum franchises so that refiners, many of whom operate nationwide, can organize their affairs without facing a "patchwork" of standards. *Senate Report* 16, 19; 124 Cong. Rec. 12,764 (1978) (statement of Sen. Jackson) ("The patchwork of these State laws has become a serious encumbrance on the franchisor-gasoline suppliers, so much so that [franchisors] are willing to accept the restrictions * * * in return for uniformity of laws across the nation."); *Mobil Oil Corp.* v. *Virginia Gasoline Marketers & Auto. Repair Ass'n*, 34 F.3d 220, 225 (4th Cir. 1994) ("Most petroleum franchisors do business in a number of states and Congress has provided [a nationwide standard] to ensure uniformity."), cert. denied, 513 U.S. 1148 (1995).

Contrary to that goal, the court of appeals prescribed a confusing and indeterminate test for deciding whether a franchisor has "terminate[d]" a franchise. The court of appeals disavowed a holding that "any material breach of the lease would necessarily be sufficient to sustain the constructive termination claim." Pet. App. 23. It indicated instead that the relevant contract breach must constitute "such a material change that it effectively ended the lease, even though the plaintiffs continued to operate the business." *Ibid.* But the court offered no workable standard for determining whether a particular contract breach has "effectively ended" the franchise when the franchisee is able and willing to continue its operations for a sustained period. Nor could the court have done so, given the essential contradiction involved in declaring "effectively ended" a franchise that is ongoing in each of its basic components. Application of the test articulated in the decision below would not lead to nationally uniform standards governing termination.

C. The Court Of Appeals' Decision Is Inconsistent With The Doctrine Of "Constructive Termination" In Other Contexts

The court of appeals' expansive reading of the word "terminate" in Section 2802(a)(1) is not supported by the general understanding of "constructive termination" doctrine in other contexts. As the court of appeals recognized, analogous common-law doctrines have traditionally "require[d] an actual severance of the relationship." Pet. App. 23. Consistent with that understanding, courts have applied the "constructive termination" concept to situations in which the challenged conduct has the practical effect of forcing an end to a particular legal relationship, even though the defendant has not formally or expressly severed his ties with the plaintiff.

In the field of employment law, for example, "[t]he employee must leave the workplace" to recover on a "constructive termination" theory. Pet. App. 23; see *Pennsylvania State Police* v. *Suders*, 542 U.S. 129, 134, 141 (2004) (to claim "constructive discharge" under Title VII of the Civil Rights Act of 1964, 42 U.S.C. 2000e *et seq.*, the employee must quit and "show that the abusive working environment became so intolerable that her resignation qualified as a fitting response"). "The inquiry is objective: Did working conditions become so intolerable that a reasonable person in the employee's position would have felt compelled to resign?" *Id.* at 141; see *Bean* v. *Wisconsin Bell, Inc.*, 366 F.3d 451, 454 (7th Cir. 2004) (Posner, J.) (Constructive termination "refers to the situation in which an employer precipitates an employee's resignation by making the employee's working conditions unbearable."). Courts have also required an "actual severance of the relationship" to establish "constructive eviction in landlord-tenant law": "the tenant must move out." Pet. App. 22-23; *Brendle's Stores Inc.* v. *OTR*, 978 F.2d 150, 155 (4th Cir. 1992) (applying South Carolina law).

Courts have adopted a similar understanding of constructive termination under the Automobile Dealers Day in Court Act (ADDCA), 15 U.S.C. 1221 *et seq.*, which resembles the PMPA to the extent it limits the circumstances in which automobile manufacturers may "terminat[e]" a dealer franchise. 15 U.S.C. 1222 (providing that an automobile dealer may recover damages caused by "the failure of [an automobile manufacturer] to act in good faith in performing or complying with any of the terms or provisions of the franchise, or in terminating, canceling, or not renewing the franchise with said dealer"). As one court of appeals has explained, the ADDCA's restrictions on termination apply "where the manufacturer forces a termination by a dealer under circumstances which would warrant a court in concluding that even though in appearance the termination was voluntary it was in fact coerced by the manufacturer." *American Motors Sales Corp.* v. *Semke*, 384 F.2d 192, 195 (10th Cir. 1967). See *Imperial Motors, Inc.* v. *Chrysler Corp.*, 559 F. Supp. 1312, 1315 (D. Mass. 1983) (following *Semke* and describing the situation as a "constructive termination").[7]

The court of appeals reasoned that comparison of the "constructive termination" concept in the PMPA context to the treatments of such claims elsewhere is "misleading" because "sunk costs, optimism, and the habit of years might lead franchisees to try to make the new arrangements work." Pet. App. 22-23. That is not, however, a meaningful distinction. "[S]unk costs, optimism, and the habit of years" are by no means unique to petroleum franchises and do not provide a sound basis for differentiating the PMPA from other con-

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[7] Courts have not specifically addressed whether the dealership must end before a dealer claims "constructive termination" under the ADDCA. In both *Semke* and *Imperial Motors*, the dealer ceased its operations before bringing suit. See *Semke*, 384 F.2d at 194-195; *Imperial Motors*, 559 F. Supp. at 1314.

texts in which the "constructive termination" theory has been applied.[8]

The rationale for recognizing a claim of "constructive termination" under the PMPA is not that courts may add to the prohibitions that Congress imposed in the text of the Act. Rather, it is that the word "terminate" in Section 2802(a)(1) is properly construed to encompass franchisor conduct that, as a practical matter, forces an end to at least one element of the franchise relationship, even though the franchisor does not expressly abrogate the parties' agreement. The soundness of that interpretation, however, depends in large measure on the longstanding recognition of the concept of "constructive termination" in analogous contexts. Cf. *Suders*, 542

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[8] Few decisions address the question whether a dealer that remains in business may claim constructive termination under state franchise laws, and those decisions do not establish a consistent rule. Compare, *e.g.*, *Coast to Coast Stores (Cent. Org.), Inc.* v. *Gruschus*, 667 P.2d 619, 623 (Wash. 1983) (holding that a franchise is terminated under the Washington Franchise Investment Protection Act "only when the agreement between the franchisee and franchisor is brought to an end, terminating the franchisee's right to use the franchisor's trade name, service mark, or the like"), with *Petereit* v. *S.B. Thomas, Inc.*, 63 F.3d 1169, 1183 (2d Cir. 1995) (holding that the franchisee did not need to be driven "out of business * * * in order to justify a finding of constructive termination" under the Connecticut Franchise Act), cert. denied, 517 U.S. 1119 (1996). Courts applying state franchise laws, however, generally describe constructive termination in terms of franchisor conduct that precludes continued operations by the franchisee. See, *e.g.*, *American Bus. Interiors, Inc.* v. *Haworth, Inc.*, 798 F.2d 1135, 1141 (8th Cir. 1986) (concluding that constructive termination occurred under Missouri franchise law when franchisor "refuse[d] to do business with [its] franchisee"); *Remus* v. *Amoco Oil Co.*, 794 F.2d 1238, 1240 (7th Cir.) (Posner, J.) (suggesting that there could be a claim for constructive termination under Section 135.03 of the Wisconsin Fair Dealership Law when the franchisor's conduct "ma[de] the dealer's competitive circumstances so desperate that the dealer 'voluntarily' gives up the franchise"), cert. dismissed, 479 U.S. 925 (1986).

U.S. at 142 (noting that "[b]y 1964, the year Title VII was enacted, the [constructive discharge] doctrine was solidly established in the federal courts"). The dealers in this case seek to use that history as a basis for reading the word "terminate" in Section 2802(a)(1) to encompass non-explicit terminations, while treating as irrelevant the limitations that courts have traditionally placed on the "constructive termination" doctrine. There is no warrant for that approach.

D. Because The Conduct At Issue Here Did Not End The Franchises, The Dealers Could Not Recover Under the Act

The dealers in these cases failed to establish that their franchises were "terminate[d]" within the meaning of Section 2802(a)(1). Where, as here, a franchisor does not explicitly terminate any of the three elements of a petroleum marketing franchise, its conduct can properly be said to "terminate" the franchise in a "constructive" sense only if a reasonable franchisee in the circumstances would be effectively compelled to abandon one (or more) of the franchise elements, as when the franchisor's conduct forecloses any reasonable possibility that the business could be operated profitably. And a franchisee cannot reasonably claim to have been subjected to such effective compulsion unless it either (a) actually ceases that aspect of its operations or (b) promptly seeks preliminary injunctive relief preventing the franchisor from carrying out its announced intent to engage in conduct that would leave the franchisee no reasonable alternative but to abandon that aspect of its operations.

None of the eight dealers in this case satisfied that standard. The withdrawal of the rent subsidy did not force an end to any element of their franchise operations. All of the dealers continued to operate their franchises for a prolonged period—in most cases, for several years—after the rent subsidy was withdrawn. And all of the dealers either signed new

agreements, or agreed to extend existing agreements, that did not include the rent subsidy. See J.A. 268-331. That continued operation precluded any reasonable finding that the withdrawal of the subsidy effectively compelled the dealers to abandon their businesses. The defendants were therefore entitled to judgment as a matter of law with respect to the dealers' constructive termination claims.

II. THE COURT OF APPEALS CORRECTLY HELD THAT A FRANCHISEE MAY NOT RECOVER FOR "CONSTRUCTIVE" NONRENEWAL UNDER THE PMPA IF IT SIGNS AND OPERATES UNDER A RENEWED FRANCHISE AGREEMENT

The court of appeals' rejection of the dealers' "constructive nonrenewal" claims was compelled by Section 2802(a)(2)'s unambiguous text, and the soundness of that ruling is confirmed by the structure and purpose of other PMPA provisions governing the nonrenewal process. Because all eight dealers in this case either signed renewed agreements or sold their businesses before the previous agreements expired, the court of appeals correctly reversed the jury verdicts in their favor on their constructive nonrenewal claims.

1. Under the PMPA, a franchisor may not "fail to renew any franchise relationship" except for specified reasons. 15 U.S.C. 2802(a)(2). The Act defines the terms "fail to renew" and "nonrenewal" as the "failure to reinstate, continue, or extend" the relationship with the franchisee. 15 U.S.C. 2801(14). A franchisor cannot reasonably be said to have "fail[ed] to renew" within the meaning of the Act if it has in fact reinstated, continued, and extended the franchise relationship by offering a renewed agreement that the franchisee has accepted. See Pet. App. 32 (rejecting the dealers' constructive nonrenewal claim because the dealers had "signed

and operate[d] under the renewal agreement complained of").

A franchisor might explicitly fail to renew a franchise relationship by advising the franchisee that it will not be offered a new agreement when the current agreement expires. The franchisor might also indirectly or "constructively" fail to renew the relationship by insisting on changes that a franchisee would be forced to reject because continued operation under such terms would not be reasonably possible. See *Abrams Shell* v. *Shell Oil Co.*, 343 F.3d 482, 488 (5th Cir. 2003); *Dersch Energies*, 314 F.3d at 864. But in either circumstance, there must be a nonrenewal; the plain terms of the Act leave no room for a claim that a franchise relationship was "constructively" nonrenewed even though the parties entered into a new franchise agreement.[9]

The dealers assert (Pet. 24-25) that they "reserve[d]" their rights under the PMPA by signing the renewal agreements "under protest." The significance of the signed renewal agreements, however, is not that they constituted waivers of the dealers' legal rights, but that they negated the possibility of actionable PMPA violations. The PMPA affords franchisees the right to sue only to challenge an unlaw-

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[9] There is relatively little statutory or common-law history for "constructive nonrenewal" claims. The concept has arisen primarily in the insurance context where a new insurance contract modified the terms of a prior contract. See, *e.g.*, *American Cas. Co.* v. *Baker*, 22 F.3d 880, 893-894 (9th Cir. 1994); *American Cas. Co.* v. *Continisio*, 17 F.3d 62, 65-67 (3d Cir. 1994); *Adams* v. *Greenwood*, 10 F.3d 568, 572 (8th Cir. 1993). In accord with the position taken here, these cases indicate that signing a modified contract "is inconsistent with [an] assertion of constructive nonrenewal." *Baker*, 22 F.3d at 893 (quoting *Adams*, 10 F.3d at 572); see *Continisio*, 17 F.3d at 66 ("Even in a state where renewal is strictly defined as continuation of coverage on the same, or nearly the same, terms as the policy being renewed, acceptance of new terms constitutes a renewal.") (citation and internal quotation marks omitted).

ful termination or nonrenewal of the franchise. See 15 U.S.C. 2805 (providing a civil action to redress noncompliance only with Section 2802, prohibiting unlawful terminations or nonrenewals, and Section 2803, governing trial and interim franchises). The Act does not furnish a dealer whose franchise is in fact renewed with a claim for other grievances about the negotiation process or the manner in which a renewal occurred. A dealer that chooses to sign an agreement with its franchisor despite dissatisfaction with its terms has nonetheless renewed the franchise relationship and has no "failure to renew" cause of action to preserve.

2. The structure and purposes of the Act confirm that an actual renewal of the franchise relationship precludes a "nonrenewal" claim. As noted earlier, the PMPA represents a delicate balance between the goal of protecting the reasonable expectations of franchisees in the continuation of their businesses and the goal of preserving "adequate flexibility" for franchisors to "initiate changes in their marketing activities to respond to changing market conditions and consumer preferences." *Senate Report* 18-19. Congress designed the Act's nonrenewal provisions specifically to address those competing concerns. The dealers' theory of "constructive nonrenewal" is incompatible with the balance that Congress struck.

a. The PMPA provisions governing nonrenewal contain two key features. First, to preserve the franchisor's flexibility to respond to market demands, the Act permits a franchisor to propose new and different contractual terms at the expiration of a franchise agreement. See *Senate Report* 32 (noting that the Act allows "renewal of the franchise relationship [to] be on different terms"). To that end, the Act provides a broader range of justifications for failing to renew a franchise relationship than for terminating an existing franchise. See 15 U.S.C. 2802(b)(3) (setting forth additional

grounds for nonrenewal). Those additional lawful grounds for nonrenewal include "[t]he failure of the franchisor and the franchisee to agree to changes or additions to the provisions of the franchise," as long as the franchisor proposed the new terms "in good faith and in the normal course of business." 15 U.S.C. 2802(b)(3)(A)(i).

Second, the Act establishes a special procedural mechanism for resolving disputes about the legality of changes or additions to the terms of the previous agreement. 123 Cong. Rec. at 10,383 (statement of Rep. Dingell) ("[T]o assure that franchisees * * * receive the meaningful protections which this Federal legislation is intended to provide and to assure that [the Act's] flexibility does not frustrate the purposes of this legislation, the bill utilizes very special enforcement mechanisms."). When the franchisor offers a renewal agreement containing new terms, the franchisee may decide to accept those terms or to reject them. If the franchisee rejects the proposed agreement, the franchisor may then choose whether to modify the terms or instead to end the franchise relationship.

A franchisor that elects not to renew a franchise relationship in these circumstances must notify the franchisee of that decision, generally 90 days before the nonrenewal will take effect. 15 U.S.C. 2804(a). The notification must be in writing, must identify the reasons for the nonrenewal and the effective date, and must include a summary of the remedies available under the PMPA. 15 U.S.C. 2804(c). Upon receipt of that notice, the franchisee may seek preliminary injunctive relief permitting it to continue operating under the preexisting agreement while it challenges the legality of the franchisor's decision. 15 U.S.C. 2805(b)(1).[10] Congress specifically

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[10] The franchisee might allege, for example, that the parties' failure to agree to changed franchise terms did not constitute a lawful basis for

prescribed a relaxed showing for obtaining such relief and required district courts to grant an injunction if that showing is made. 15 U.S.C. 2805(b)(2); see pp. 2-3, *supra*.

b. The "constructive nonrenewal" theory the dealers espouse, under which a franchisee may enter into a renewed agreement "under protest" and later allege a "nonrenewal," would seriously undermine this scheme in at least three respects. First, as suggested above, that theory would expand the Act's coverage to encompass a broad range of conduct that does not actually result in the end of the franchise relationship. Second, the dealers' argument would replace the procedural mechanism Congress created with a fundamentally different scheme. Under the balance struck by Congress, the franchisee must either sign or reject a proposed renewal agreement, and a franchisor faced with a rejection may then choose either to modify the objectionable terms or give notice of nonrenewal. The procedure the dealers propose would invert that system. It would permit a dealer to execute a new agreement "under protest," thereby granting the franchisee the option either to continue operating under the new agreement or, if the terms later proved unfavorable, to challenge it as a "constructive nonrenewal." As the court of appeals observed, the franchisee would gain the benefit of the contract with nothing to lose, even if it later sued and "its claims were rejected by the courts." Pet. App. 30.

Third, the dealers' theory would frustrate Congress's intent that renewal disputes be resolved before any new agreement takes effect. That scheme furthers Congress's

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nonrenewal because the proposed changes were not "the result of determinations made by the franchisor in good faith and in the normal course of business," 15 U.S.C. 2802(b)(3)(A)(i), or because the proposed changes were made "for the purpose of converting the leased marketing premises to operation by employees or agents of the franchisor for the benefit of the franchisor," 15 U.S.C. 2802(b)(3)(A)(ii).

goal of giving franchisors flexibility to implement efficient marketing changes, *Senate Report* 19, by providing certainty about the validity of a renewed agreement containing modified terms. Allowing a franchisee to challenge such an agreement after executing it would destroy that certainty. And because the PMPA has a one-year statute of limitations, 15 U.S.C. 2805(a), the prospect of a "constructive nonrenewal" claim would "extend the period of uncertainty through the entire first year of a [renewal] contract," which in many cases is only a few years in duration. Pet. App. 30. Franchisors might respond by refraining from proposing new terms that reflect a more efficient strategy, or by "abandon[ing] the [franchise] model entirely." *Id.* at 31. In the long term, that result could cause considerable harm to consumers who may absorb the increased distribution costs through higher fuel prices. See generally *Atlantic Richfield Co.* v. *USA Petroleum Co.*, 495 U.S. 328, 343 n.13 (1990) ("[T]he public is not served by forcing [a] manufacturer to abandon [the most efficient means of distribution].").

c. The dealers contend that, by prohibiting the franchisee from claiming nonrenewal after it has signed a renewal agreement, the decision below forces franchisees "to choose between accepting an unlawful and coercive contract in order to stay in business and rejecting it and going out of business in order to preserve a cause of action." Pet. 20 (citation omitted). That contention ignores Congress's provision of a remedial mechanism tailored to the situation the dealers describe. As explained above, see pp. 25-26, *supra*, a franchisee need not go out of business in order to challenge a franchisor's "take it or leave it" offer to renew on modified terms. Rather, the franchisee may refuse the offer and seek a preliminary injunction allowing it to continue operating on the terms of the previous agreement while the litigation proceeds. See *Dersch Energies*, 314 F.3d at 863; 2 W. Michael

Garner, *Franchise and Distribution Law and Practice* § 15:10, at 15-37 to 15-38 (Sept. 2003) ("The plain language of the PMPA contemplates an actual ending of the franchise relationship * * * . A franchisee who is presented with a new agreement that is so coercive that it suggests that the franchisor has an ulterior motive to prevent renewal can refuse the agreement and then move for a preliminary injunction under the Act.").

There is also no merit to the dealers' argument (Pet. 21) that the PMPA's remedial scheme is ineffective because few franchisees have the financial resources to bring suit to forestall an unlawful nonrenewal. The PMPA allows successful dealers to recover attorneys' fees, expert costs, compensatory damages, and, in some circumstances, punitive damages. 15 U.S.C. 2805(d)(1). Such provisions are normally considered sufficient to encourage suit. Cf. *City of Riverside* v. *Rivera*, 477 U.S. 561, 578 (1986) ("The function of an award of attorney's fees is to encourage the bringing of meritorious civil rights claims which might otherwise be abandoned because of the financial imperatives surrounding the hiring of competent counsel.") (quoting *Kerr* v. *Quinn*, 692 F.2d 875, 877 (2d Cir. 1982)). And even if some dealers face economic difficulty in pursuing the remedies that the PMPA provides, that fact cannot justify holding the franchisor liable for "fail[ing] to renew [the] franchise relationship," 15 U.S.C. 2802(a)(2), when no failure to renew has actually taken place. Dealers in these circumstances may have a claim against the franchisors under state law, but not under the explicit terms of the PMPA.

3. The dealers in this case did not establish that the defendants "fail[ed] to renew" their franchise relationships within the meaning of the PMPA. The evidence at trial showed that seven of the eight dealers signed and operated under renewal agreements, and that the eighth dealer sold

his franchise before the franchise term expired. See Shell Br. 10-11. The court of appeals therefore correctly granted judgment to the defendants on the dealers' "constructive nonrenewal" claims.

CONCLUSION

The judgment of the court of appeals should be reversed with respect to the dealers' "termination" claims and affirmed with respect to the dealers' "nonrenewal" claims.

Respectfully submitted.

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